COMMONWEALTH OF VIRGINIA

STATE CORPORATION COMMISSION

AT RICHMOND, DECEMBER 19, 2001

APPLICATION OF

KENTUCKY UTILITIES COMPANY CASE NO. PUE010003

For approval of a functional separation plan

FINAL ORDER

On December 29, 2000, Kentucky Utilities Company (the "Company"), filed with the State Corporation Commission ("Commission") an application for approval of the Company's plan for functional separation of its generation assets from its retail transmission and distribution assets. This application was submitted pursuant to § 56-590 B of the Virginia Electric Utility Restructuring Act (the "Act"), Chapter 23 (§ 56-576 et seq.) of Title 56 of the Code of Virginia (the "Code"), and the Commission's Regulations Governing the Functional Separation of Incumbent Electric Utilities Under the Virginia Electric Utility Restructuring Act (the "Functional Separation Rules"), 20 VAC 5-202-10 et seq.

The Act requires each incumbent electric utility in Virginia to submit a plan for the functional separation of the utility's generation, transmission, and distribution assets and operations. The Functional Separation Rules govern the relationships between affiliated functionally separated entities, the Commission's oversight of such affiliated companies, and the requirements of the functional separation plans submitted by each incumbent electric utility.

The Company, which conducts business in Virginia under the name Old Dominion Power ("ODP"), stated in its application that, with the exception of one 500 kV transmission line, all of ODP's generation and transmission assets are located in Kentucky and are subject to the jurisdiction of the Kentucky Public Service Commission ("Kentucky PSC").[1] The Company argued that legally and practically it cannot functionally separate its assets related to its Virginia load nor transfer them to an affiliated entity. ODP suggested in its application, however, that it can achieve the goals and objectives of the Act without functional separation.

First, ODP proposed to operate under the guidelines set forth by the 1999 Kentucky General Assembly in Kentucky House Bill 897 which imposes a code of conduct on the relationship between regulated entities and unregulated affiliates and establishes specific reporting requirements. Second, ODP proposed to file with the Commission the reports it is required to file with the Kentucky PSC. Third, ODP stated that it would continue to operate pursuant to the Services Agreement approved

[1] ODP has local and sub-transmission facilities, a 500/161 kV substation and 161 kV and 69 kV lines, in Virginia. As discussed later in this Order, such facilities are classified as distribution.

by the Commission in Motion of Kentucky Utilities Company, For order regarding allocation factors, Case No. PUA000050. Finally, ODP filed a cost of service study and revised tariff sheets to unbundle retail rates into transmission and distribution components to be available on and after January 1, 2002.

On February 5, 2001, the Commission issued an Order for Notice and Inviting Comments and Requests for Hearing that established the procedural schedule for this matter. The Company was directed to publish notice of its application and to serve notice on local officials,[2] and dates were established for filing comments and/or requests for hearing.[3] In addition, the Order directed the Commission Staff ("Staff") to review the application and to file a report presenting its findings and recommendations.[4]

On August 27, 2001, Staff filed its Report. Staff recommended that the Commission:

(1) Approve the Company's plan as modified by the changes recommended by Staff in the Report;

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[2] On March 30, 2001, the Company filed proof of notice in compliance with our February 5, 2001, Order.

[3] No comments or requests for hearing were filed by the respective March 30, 2001, and April 6, 2001, deadlines.

[4] On June 7, 2001, Staff filed a motion to extend the deadline for filing the Staff Report from June 27, 2001, to August 27, 2001, and to establish September 10, 2001, as the deadline for the Company to file any comments in

(2) Adopt Staff's jurisdictional adjustments to ODP's per books cost of service study as reflected by Attachment I to the Staff Report, Attachment II to the Staff Report which shows a breakdown of revenue and expense by function incorporating Staff adjustments, and Attachment III to the Staff Report which shows breakdown of rate base allocated to the function incorporating Staff's adjustment to the Report;

(3) Adopt the Staff's adjusted rate design methodology to maintain actual rate of return by rate schedules as reflected by Attachments IV and V to the Staff Report and to reflect Staff's recommended shift the difference between the Federal Energy Regulatory Commission ("FERC") based transmission revenue requirement and the Virginia retail class transmission revenue requirement from the unbundled distribution rates to capped generation rates; and

(4) Require, when the Company enters into competitive services in Virginia, ODP to file a code of conduct outlining its plan to comply with the Virginia requirements governing affiliate and/or division relationships and to file any waivers necessary or desired.

Following the filing of the Staff Report, Staff and the Company entered into discussions regarding Staff Recommendation (3). Staff made this recommendation based on Staff's objection

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response to the Staff Report. On June 12, 2001, the Commission entered an to KU's proposal to shift the difference between the FERC and Virginia transmission revenue requirements to the distribution function instead of the generation function. Staff recommended that KU recompute its rates consistent with a per class adjustment from distribution to generation contained in the Staff Report.

Upon review of the Staff Report, KU noted that in the functionally separated cost of service study submitted in its original application, the Company's local and sub-transmission facilities in Virginia, consisting of a 500/161 kV substation and 161 kV and 69 kV lines, were identified separately under the transmission function. While allocated to the transmission function in the cost study, the cost associated with those facilities was assigned to the unbundled distribution rates in the Company application consistent with Commission approved historical allocation of such facilities to the Virginia bundled distribution function.

On October 9, 2001, KU filed comments and an amended application with the Commission containing revised responses to Staff interrogatories and revised attachments to support the reclassification of the 500/161 kV substation and 161 kV and 69 kV lines to distribution facilities.[5] Classified pursuant to

order granting the motion for extension.

[5] On September 14, 2001, the Commission granted the Company’s motion to extend the deadline for filing its comments to September 28, 2001. On September 28,

FERC guidelines, the Company's 500 kV line remained in the transmission function. The difference between the FERC and Virginia transmission revenue requirements was incorporated into the generation, rather than the distribution, function.

On November 8, 2001, Staff filed, on behalf of itself and the Company, a Stipulation setting forth the parties' agreement on the reassignment of the local and sub-transmission facilities and their inclusion as part of the distribution function in the unbundled rate design. As noted above, the Company's 500 kV line remains assigned to the transmission function. The Stipulation also notes the incorporation of the transmission revenue requirement difference into the generation function. The parties agree to revised interrogatory responses and corresponding revised attachments amending the Company's application. The parties also accept revised Attachments to the Staff Report submitted by the Company. Finally, the Stipulation contains revised rate schedules that Staff and the Company urge the Commission to adopt.

NOW THE COMMISSION, having considered the Staff Report and the Stipulation filed herein, is of the opinion and finds that the Stipulation should be accepted, and that the recommendations

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2001, the Commission granted the Company’s motion for a further extension to October 9, 2001.

contained in the Staff Report as modified by the Stipulation should be adopted.

Accordingly, IT IS ORDERED THAT:

(1) The Stipulation filed by Staff and the Company is hereby accepted.

(2) The recommendations contained in the Staff Report as modified by the Stipulation are hereby adopted.

(3) The Company's plan for functional separation is approved as modified herein.

(4) The Company's revised rate schedules attached to the Stipulation as Exhibit 1 are hereby accepted.

(5) This case is closed, and the papers shall be placed in the file for ended causes.